

# Electric Utility Rate Case Regulation

Presentation to the  
House Committee on Energy and Technology

Michigan Public Service Commission  
February 26, 2013



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## The Union Carbide decision

- “The Public Service Commission possesses no ‘common law’ powers.....As a creature of the Legislature, the commission possesses only that authority bestowed upon it by statute.”
- *Union Carbide v PSC*, 431 Mich 135 (1988)



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## Major Substantive Laws giving the Commission its jurisdiction

- Railroad Act (1909)
- Transmission of Electricity Act (1909)
- Public Utilities Commission Act (1919)
- Carriers by Water Act [a/k/a Ferry Boats] (1921)
- Certificates of Convenience and Necessity Act (1929)
- **Public Service Commission Act** (1939)
- Protection of Underground Facilities (1974)
- Michigan Telecommunications Act (1991)
- Electric Transmission Line Certification Act (1995)
- Customer Choice and Reliability Act (2000)
- Video Franchising Act (2006)
- Clean, Renewable, and Efficient Energy Act (2008)



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## Major Procedural Laws governing the Commission

- Administrative Procedures Act (1969)
- Open Meetings Act (1976)
- Freedom of information Act (1976)
- Costs of Regulating Utilities Act (1972)



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## Ratemaking

- Ratemaking is quasi-judicial & quasi-legislative.
- US Constitution, Amendment V., states:
  - “...nor shall private property be taken for public use, without just compensation.”



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## Utility Rate Regulation in Michigan

- Periodically, the MPSC examines a utility's costs and revenues in a rate case proceeding. Usually, the utility is asking for higher rates to cover increases in its costs.
- Annually, the MPSC conducts power supply cost recovery (PSCR) plan and reconciliation proceedings, which focus only on fuel and purchased power costs and transportation charges.



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## "Social Compact"

### Customers:

- Obligation to serve all customers' needs
- Just and reasonable rates
- Abundant, safe, and reliable service

### Utilities:

- Right to recover all reasonable and prudently incurred costs
- Opportunity to earn a reasonable rate of return on its capital investments



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## Ratemaking Principles

MPSC is not bound to the use of any single formula or combination of formulae in determining rates.

Although rates must be just and reasonable, it is the result reached, not the method employed, which is controlling.

Once established, rates are presumed to be just and reasonable.



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## Ratemaking Procedures

(Reflecting modifications under PA 286)

- Utility Application Filing
  - 30 days to determine completeness
  - Notice throughout service territory
  - Prehearing conference set by Commission
  - 180 day clock for self-implementation starts ticking (File and Use Rates)
  - Scheduling set which allows final order within twelve months



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## Ratemaking Procedures

- Self Implementation date (180 days)
  - Unless for good cause, the commission issues a temporary order preventing rate increase.
- Evidentiary Hearings by MAHS ALJ
  - Utility case filing (application)
  - Discovery
  - Staff and intervener cases filed
  - Rebuttal evidence
  - Cross examination of all parties



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## Ratemaking Procedures

- Briefs and Reply Briefs to ALJ
- Proposal for Decision by ALJ
- Exceptions and Replies to Exceptions
- Final Order within 12 months of Application filing
- Appeals to Court of Appeals
  - If utility self-implemented a rate increase and over-collected, a refund is required, with interest.



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## Energy Legislation in 2008

- PA 286
  - File and Use Rates
  - Twelve month “hard cap” for final order
  - Merger and Acquisition Review Authority
  - Certificate of Need for New Generation – Integrated Resource Planning
  - Cap on Customer Choice Levels
  - Rate Alignment with Cost of Service (Deskewing)



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## The Substance of Ratemaking

- Ratemaking is intended to be a proxy for competition in a competitive marketplace



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## A sampling of the issues typically raised in a rate case

- Test year [a 12 month period & how to select the data]
- Rate base
  - Net utility plant
  - Working capital
  - Land held for future use



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This very simplified rate formula is intended to produce a utility's revenue requirement:

$$R = O + (V - D)r$$

- R is the utility's total revenue requirement or rate level. This is the total amount of money a regulator allows a utility to earn.
- O is the utility's operating expenses.
- V is the gross value of the utility's tangible and intangible property.
- D is the utility's accrued depreciation. Combined (V - D) constitute the utility's rate base, also known as its capital investment.
- r is the rate of return a utility is allowed to earn on its capital investment or on its rate base.



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## Issues, continued:

- Overall rate of return
  - Capital structure
  - Cost rates
    - Common equity [10.7%]
    - Long-term debt [5.62%]
    - Short-term debt [5.68%] & preferred stock [4.46%]
    - Deferred income tax credit [0.00%]
    - Deferred investment tax credit [0.00%]
    - Deferred federal income tax [0.00%]
    - Overall return [6.93%]



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## Issues, continued:

- Adjusted Net Operating Income
  - Jurisdictional revenues
  - Fuel & purchased and net interchanged power
  - Discount fees on accounts receivables
  - Employee Incentive Compensation Plan
  - Dues and Lobbying expenses
  - Billing system cost subsidy
  - Tree trimming costs and tracker
  - Pension costs and OPEB tracker
  - Incremental environmental compliance costs
  - Pro-forma tax adjustment



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## Calculation of Base Rate Sufficiency

• Rate Base	\$5,013,880,000
• Rate of Return	6.93%
• Income Required	\$347,462,000
• Adjusted NOI	\$379,926,000
• Income excess	\$29,464,000
• Revenue multiplier	1.5683
• Revenue excess	\$46,208,400



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## Issues, continued:

- Other Revenue Issues
  - Zeeland plant revenue issues
    - Interim relief order granted \$69.5 million to be collect via a surcharge, not through base rates
    - Final order approved an additional \$4.177 million
    - Palisades transaction costs
    - Palisades refund to Rate E-1 customers
    - Energy Efficiency Proposal
    - Electric Choice Incentive Mechanism
    - Nuclear legacy costs
    - **REVENUE DEFICIENCY -- \$27,468,000**



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## Questions?

[www.michigan.gov/mpsc](http://www.michigan.gov/mpsc)



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